

1 KAREN A. OVERSTREET
Chief Bankruptcy Judge
2 United States Courthouse
700 Stewart St., Suite 6310
3 Seattle, WA 98101
206-370-5330
4

5
6 IN THE BANKRUPTCY COURT OF THE UNITED STATES FOR
THE WESTERN DISTRICT OF WASHINGTON
7 AT SEATTLE

8 In re

Chapter 7

9 DOUGLAS SIMONSON and KAREN
10 SIMONSON,

Case No. 04-15846

11 Debtors.

12 MICHAEL MCCARTY, solely in his
13 capacity as Trustee for the
estate of Douglas and Karen
Simonson,

Adversary No. 06-01235

14 Plaintiff,

NOT FOR PUBLICATION

15 vs.

16 GLOBAL FINANCIAL SOLUTIONS,
17 LLC., et al.

MEMORANDUM DECISION ON
TRUSTEE'S MOTION FOR
SANCTIONS AGAINST HERMAN
RECOR ARAKI KAUFMAN
SIMMERLY & JACKSON PLLC

18 Defendants.

19 This matter came before the Court on the Trustee's Motion
20 for Sanctions for Violations of Discovery Rules ("Sanctions
21 Motion"), filed by the trustee, Michael McCarty (the
22 "Trustee"), against Herman Recor Araki Kaufman Simmerly &
23 Jackson PLLC ("Herman Recor"), prior counsel herein for
24 defendants Michael and Rowan Levenhagen, Mark and Sylvia Laing,
25 and David and Nancy Laning (collectively, the "Transferee
26 Defendants"). The Sanctions Motion was originally set for

MEMORANDUM DECISION - 1

1 hearing on June 13, 2008, but the Court continued the hearing
2 at Herman Recor's request to July 11, 2008. The Court heard
3 oral argument on the Sanctions Motion on that date and asked
4 the parties for supplemental materials. Subsequent to the
5 hearing, the Trustee submitted a Supplemental Declaration in
6 support of the Sanctions Motion (Docket no. 368). Herman Recor
7 submitted the following supplemental pleadings which the Court
8 has considered in connection with this ruling:

9 Declaration of Zeshan Q. Khan Regarding Declarations of
10 Robert Jackson, Patti Jackson and Dave Carlile (Docket no.
370)

11 Declaration of Robert Jackson In Response to Declarations
12 of Robert Dainard and Marc Stern (Docket no. 371)¹

13 Declaration of Patti Jackson (Docket no. 372)

14 Declaration of Dave Carlile (Docket no. 374)

15 Declaration of Cynthia A. Kuno in Support of Herman Recor
16 Araki Kaufman Simmerly & Jackson PLLC's Memorandum
Regarding Trustee's Reasonable Fees Related to Discovery
Omissions (Docket no. 375)

17 Second Declaration of Cynthia A. Kuno in Support of Herman
18 Recor Araki Kaufman Simmerly & Jackson PLLC's Memorandum
Regarding Trustee's Reasonable Fees Related to Discovery
19 Omissions (Docket no. 376)

20 Third Declaration of Cynthia A. Kuno in Support of Herman
21 Recor Araki Kaufman Simmerly & Jackson PLLC's Memorandum
Regarding Trustee's Reasonable Fees Related to Discovery
Omissions (Docket no. 377)

22
23 ¹

24 The declarations of Robert Jackson, Patti Jackson, and Dave
25 Carlile listed above were filed in response to allegations in
the Trustee's Reply brief (Docket no. 359) regarding a real
26 estate transaction in Chelan, Washington involving
Mr. Jackson and Robert Dainard. The Court does not believe
this transaction is germane to the issues raised in the
Sanctions Motion and accordingly has not considered the
declarations relating to the transaction.

1 Declaration of Cynthia A. Kuno re After-Hours Filing of
2 Memorandum Regarding Trustee's Reasonable Fees Related to
Discovery Omissions (Docket no. 379)

3 Memorandum of Herman Recor Araki Kaufman Simmerly & Jackson
4 PLLC Regarding Trustee's Reasonable Fees Related to
Discovery Omissions (Docket no. 378)

5 Correspondence dated September 15, 2008, from Cynthia Kuno
6 (Docket no. 382)

7 For the following reasons, the Court will order Herman
8 Recor to pay compensatory sanctions to the Trustee in the sum
9 of \$183,359.43 pursuant to Fed.R.Civ.P. 26(g)(3).

10 I. JURISDICTION

11 The Court has jurisdiction of this matter pursuant to 28
12 U.S.C. § 157(a) and (b) and § 1334(a) and (b). This is a core
13 proceeding under 28 U.S.C. § 157(b)(2)(A).

14 II. BACKGROUND

15 A. Summary of the Transactions at Issue.

16 Douglas and Karen Simonson (the "Debtors") filed a
17 chapter 7 petition on April 29, 2004, Case no. 04-15846 (the
18 "Main Case"). The Trustee commenced this adversary proceeding
19 on April 29, 2006, seeking money or the return of property of
20 the estate allegedly transferred by the Debtors to the
21 Transferee Defendants. As of the petition date, the Debtors
22 owned two pieces of real property on Lake Washington, their
23 residence located at 11609 Holmes Point Drive, Kirkland,
24 Washington (the "11609 Property") and an adjacent rental
25 residence located at 11615 Holmes Point Drive N.E., Kirkland,
26 Washington (the "Rental Property"). On June 30, 2004, the
Debtors filed a motion in the Main Case to compel the Trustee

1 to abandon both properties on the grounds that the properties
2 lacked equity for the creditors and were burdensome to the
3 estate. In support of the motion, counsel for the Debtors
4 filed a declaration attached to which was the first page of an
5 appraisal valuing the 11609 Property at \$820,000, the Debtors'
6 Schedule D showing secured liens against the 11609 Property in
7 excess of the value of the property, and a copy of a purchase
8 and sale agreement pursuant to which Global Financial Solutions
9 ("GFS") would purchase the 11609 Property from the Debtors for
10 \$800,000. The Court entered an unopposed order of abandonment
11 on July 13, 2004 abandoning both properties (the "Abandonment
12 Order"). The Debtors' transfer of the Rental Property
13 subsequent to the entry of the Abandonment Order is not
14 relevant to the issues in the Sanctions Motion and therefore
15 will not be described in detail. The Debtors' transfers of the
16 11609 Property, however, are relevant and will be described in
17 detail below.

18 The 11609 Property was initially transferred by the Debtors
19 to the Levenhagens in November of 2004, about four months after
20 entry of the Abandonment Order and seven months after the
21 petition date. Prior to filing bankruptcy, however, the
22 Debtors had filed an application for a short plat and boundary
23 line adjustment affecting both the 11609 Property and the
24 Rental Property. The application was approved by the county
25 after the Abandonment Order was entered. Pursuant to the
26 approved short plat, 1,745.8 square feet of property from the
Rental Property was moved to the 11609 Property and the 11609

1 Property was then divided into two lots. The new lot was
2 described as 11611 Holmes Point Drive, Kirkland, Washington
3 (the "1611 Property"). The short plat was completed on June 1,
4 2005. The short plat application was not disclosed in the
5 Debtors' bankruptcy papers or in the Debtors' motion for
6 authority to abandon the 11609 Property.

7 In a series of transactions that took place in June of 2005
8 involving the Debtors' wholly-owned limited liability company,
9 Network Builders, LLC ("Network"), the Debtors transferred
10 Network to the Levenhagens, the Levenhagens deeded the 11609
11 Property to Network, and then the Levenhagens transferred
12 Network (which then owned the 11609 Property) back to the
13 Debtors. The day after the Levenhagens transferred Network
14 back to the Debtors, Mr. Simonson executed a deed of trust on
15 behalf of Network in favor of Daniels Capital, LLC ("Daniels
16 Capital") in exchange for \$167,775.56. On December 9, 2005,
17 Network transferred the 11609 Property by quit claim deed to
18 the Laings and on December 22, 2005, Network transferred the
19 11611 Property by quit claim deed to David Laning.

20 With the foregoing summary of the transactions at issue,
21 the Court turns to the Trustee's specific contentions.

22 B. The Adversary Proceeding.

23 The Trustee's initial complaint ("Complaint") was filed on
24 April 29, 2006, and named as defendants GFS, David Langford,
25 Mark Hodges & Associates, Daniels Capital, and the Transferee
26

1 Defendants.² The Debtors were not initially named as defendants
2 in the Complaint. The Complaint alleged that despite the
3 representations to the Court that the 11609 Property was being
4 sold to GFS for \$800,000 pursuant to a short sale, on July 30,
5 2004, the Levenhagens had entered into a Specific Buying
6 Agreement (the "SBA") pursuant to which they agreed to purchase
7 the 11609 Property as nominees for GFS for not more than \$1.2
8 million. Pursuant to the terms of the SBA, the Levenhagens
9 were to use their credit to provide financing for the purchase
10 of the 11609 Property and, subsequent to the purchase, GFS was
11 to pay the Levenhagens \$27,972 to hold title to the 11609
12 Property for no more than 18 months. During that 18-month
13 period, GFS was to make payments on the Levenhagens' mortgage
14 debt against the 11609 Property.

15 The Complaint stated at paragraph 4.9: "Upon information
16 and belief the Trustee alleges that the debtors knew of and
17 were involved in the preparation and execution of the 11609
18 SBA." The Complaint further alleged that escrow records
19 revealed that on November 24, 2004 there was a "paper" sale of
20 the 11609 Property from the Debtors to GFS, but the King County
21 property records reflected only a sale from the Debtors to the
22 Levenhagens for \$1 million. Paragraph 4.31 of the Complaint
23 stated "Upon information and belief the Trustee alleges that
24 the Levenhagens allowed the debtors and GFS to use their credit
25 and their name to effectuate a fraud upon the Bankruptcy Court
26

² Other defendants are named in the action but are not
relevant to the Sanctions Motion.

1 in exchange for a payment of \$27,972.00 as set forth in the
2 11609 SBA." The Complaint set out the various transfers of the
3 11609 Property and the 11611 Property which are summarized
4 above. It was upon the foregoing allegations that the Trustee
5 based his Complaint to vacate the Abandonment Order and sought
6 a recovery from the Transferee Defendants under Bankruptcy Code
7 §§ 542, 543, 549, 550, and 551.

8 The Levenhagens retained Herman Recor in June of 2006 at
9 the suggestion of Mr. Simonson, who indicated that Herman Recor
10 was familiar with the "GFS situation." Declaration of Michael
11 Levenhagen in Support of Plaintiff's Motion for Sanctions
12 Against Herman Recor Araki Kaufman Simmerly & Jackson, PLLC for
13 Discovery Violations (Docket no. 329)("Levenhagen Decl.")).
14 Shortly thereafter, at the request of Herman Recor attorney
15 Robert Jackson, on June 20, 2006, Mr. Levenhagen sent Herman
16 Recor a 25 page fax which contained a summary of events related
17 to the 11609 Property and short answers to specific statements
18 in the Trustee's Complaint. *Id.* Mr. Levenhagen sent a second
19 fax to Herman Recor on June 20, 2006, which consisted of 25
20 pages including the purchase and sale agreement between the
21 Levenhagens and Network, the quit claim deed transferring the
22 11609 Property, and the Network purchase and sale agreement
23 transferring Network back to the Debtors. *Id.* By email on
24 June 22, 2006, Mr. Jackson requested that Mr. Levenhagen send
25 him any documents related to closing such as escrow
26 instructions, loan documents, etc. Levenhagen Decl., Ex. 1.
On June 23, 2006, Mr. Levenhagen sent "substantial documents"

1 related to the 11609 Property to Herman Recor via Federal
2 Express. *Id.* at ¶ 10. This documentation included a copy of
3 the Global Financial Solutions Buying Partner General Terms of
4 Agreement (the "General Buying Partner Agreement"), on which
5 Mr. Levenhagen had written "Doug Simonson" on page 5 near the
6 signature line to indicate that Mr. Simonson was the
7 Levenhagens' contact at GFS. *Id.* at 11. Mr. Levenhagen also
8 wrote in his and his wife's names as the buying partners. A
9 copy of the marked-up General Buying Partner Agreement that
10 Mr. Levenhagen sent to Herman Recor on June 23, 2006 is
11 attached to the Levenhagen Decl. as Exhibit 12.

12 On July 17, 2006, Herman Recor entered its appearance in
13 the adversary on behalf of each of the Transferee Defendants.
14 On July 21, 2006, Herman Recor also filed a motion to dismiss
15 under Rule 12(b)(6), Fed.R.Civ.P., on behalf of these
16 defendants. The Trustee opposed the motion; and at the hearing
17 on September 1, 2006, the Court denied the motion and ordered
18 the Trustee to join the Debtors in the action. On September 6,
19 2006, the Trustee filed an amended complaint adding the Debtors
20 as additional defendants.

21 On September 27, 2006, the Trustee served on Herman Recor
22 the First Request for Production of Documents for Michael and
23 Rowan Levenhagen (the "Levenhagen Requests"). At the same
24 time, the Trustee also served on Herman Recor the First Request
25 for Production of Documents for Mark and Sylvia Laing ("Laing
26 Requests") and the First Request for Production of Documents
for David and Nancy Laning ("Laning Requests") (together with

1 the Levenhagen Requests, hereinafter referred to as the "First
2 Requests"). See Exs. 1, 2, 3 to Declaration of Denise Moewes
3 in Support of Trustee's Motion for Sanctions, Docket no. 330
4 ("Moewes Decl."). The Levenhagen Requests sought production of
5 all documents in the Levenhagens' possession relating to GFS,
6 David Langford, the Laings, the Debtors, and Network, including
7 emails, letters and correspondence. *Id.*, Ex. 1.

8 Although answers to the First Requests were due on
9 October 27, 2006, it was not until October 26, 2006 that
10 Mr. Levenhagen received an email from Robert Jackson indicating
11 that the Trustee had asked for copies of any correspondence
12 between the Levenhagens and the Debtors, including emails.
13 Levenhagen Decl. at ¶12. Mr. Levenhagen compiled all
14 responsive emails through January of 2006. Because the 11609
15 Property had been sold in December of 2005, Mr. Levenhagen did
16 not assemble emails subsequent to that date believing they
17 would not be responsive. Mr. Levenhagen also did not produce
18 any emails referencing Network because Mr. Jackson had not
19 requested those. However, the Trustee had specifically
20 requested all documents mentioning the Simonsons or Network in
21 Request for Production No. 2 of the Levenhagen Requests.
22 Moewes Decl., Ex. 1.

23 On October 30, 2006, Mr. Levenhagen sent the emails and
24 correspondence contained in Exhibits 3 and 4 to the Levenhagen
25 Decl. to Mr. Jackson by Federal Express. Levenhagen Decl.,
26 ¶15. This package included 27 pages of emails and faxes that
Mr. Levenhagen had previously printed (the print date shows at
MEMORANDUM DECISION - 9

1 the bottom of the page of each email)(Levenhagen Decl., Ex. 3),
2 and 66 pages of emails Mr. Levenhagen printed on October 28,
3 2006 (Levenhagen Decl., Ex. 4)(the foregoing emails and faxes
4 will hereinafter be referred to as the "November 1 2006
5 Documents"). Excluding duplicate emails, the November 1 2006
6 Documents included 119 emails and faxes. Mr. Levenhagen never
7 received from Herman Recor a copy of the Levenhagen Requests
8 and he was never advised by anyone at Herman Recor that
9 additional emails or correspondence were required to be
10 produced. *Id.*, ¶17. Herman Recor did not turn over the
11 November 1 2006 Documents to the Trustee in response to the
12 Levenhagen Requests.

13 On October 13, 2006, Herman Recor filed a motion for
14 summary judgment to dismiss the Trustee's claims against the
15 Transferee Defendants (the "First Motion for Summary Judgment,"
16 Docket no. 37). A hearing on that motion was initially set for
17 November 3, 2006. On October 24, 2006, the Debtors, through
18 their counsel Greg Cavagnaro, also filed a motion for summary
19 judgment which was scheduled for hearing on November 17, 2006
20 (the "Debtors' Summary Judgment Motion," Docket no. 50). As of
21 October 31, 2006, however, because Herman Recor had not
22 responded to the First Requests the Trustee sought a
23 continuance of the First Motion for Summary Judgment. Moewes
24 Decl., Ex. 8. In an email dated October 27, 2006, Ms. Leanne
25 Volz, a paralegal at Herman Recor, advised Ms. Denice Moewes,
26 Trustee's counsel, that she was assembling documents responsive
to the First Requests but needed additional time to produce the

1 documents because Mr. Stephen Araki, lead counsel for the
2 Transferee Defendants, was out of the country. The First
3 Motion for Summary Judgment was continued to November 17 and
4 finally to December 1, 2006. Similarly, the hearing on the
5 Debtors' Summary Judgment Motion was continued to December 1,
6 2006. As of November 6, 2006, Ms. Moewes was still seeking a
7 response to the First Requests from Mr. Araki. See 11/6/06
8 email from Moewes to Araki, Moewes Decl., Ex. 9.

9 On November 7, 2006, the Trustee finally received the
10 Levenhagens' response to the First Requests (the "First
11 Response"). Moewes Decl., ¶ 13, Ex. 10. The First Response
12 included general objections that the First Requests were over
13 broad and "invasive of the attorney client privilege," but
14 there was no indication in the First Response that documents
15 had been withheld on the ground of privilege or for any other
16 reason. *Id.*, Ex. 10. In response to Request for Production
17 No. 2, the First Response stated: "Defendants are producing
18 documents that are responsive to this request that have been
19 located to date. Defendants are continuing to look for any
20 additional documents that may be responsive and will provide
21 any additional records located." *Id.*, Ex. 10. None of the
22 November 1 2006 Documents were included in the documents
23 attached to the First Response. Also missing from the response
24 were two limited liability company purchase and sale agreements
25 related to the sale of Network to the Levenhagens and the quit
26 claim deed transferring the 11609 Property from the Levenhagens
to Network. Neither the SBA nor the General Buying Partner

1 Agreement were turned over. All of these documents, including
2 the November 1 2006 Documents (hereinafter referred to
3 collectively as the "Withheld Documents"), were in the
4 possession of Herman Recor when the First Response was made.
5 At no time did Herman Recor prepare or provide to the Trustee a
6 privilege log indicating that documents had been withheld from
7 production.

8 Also on November 7, 2006, Herman Recor produced documents
9 it deemed responsive to the Laing Requests and the Laning
10 Requests. Although the production in response to the Laing
11 Requests included a copy of the general and specific buying
12 partner agreement between the Laings and a company called New
13 Century Builders, Inc. ("New Century"), Herman Recor did not
14 produce similar agreements for the Lanings. Moewes Decl., ¶¶
15 14, 16, Exs. 11, 12.

16 Because counsel for the Trustee suspected that the Lanings
17 were parties to a buying partner agreement, Mr. Edmund Wood,
18 attorney for the Trustee, left Mr. Araki a voicemail message on
19 November 8 or 9 of 2006 requesting production of any such
20 documents. See Declaration of Edmond J. Wood in Support of
21 Trustee's Motion for Sanctions Against Herman Recor for
22 Discovery Violations, filed April 22, 2008, Docket no. 327.

23 During the same time period, early November 2006,
24 Ms. Moewes had been attempting to schedule the depositions of
25 the Transferee Defendants. She was reluctant to schedule the
26 depositions until she was satisfied that all relevant documents
had been produced. Moewes Dec., Exs. 13, 14, 15. Attached to
MEMORANDUM DECISION - 12

1 a November 14, 2006 email from Mr. Araki to Ms. Moewes were
2 copies of the first five pages of the buying partner agreement
3 between the Lanings and Lake Front Development, Inc. ("Lake
4 Front"). The signature page, however, was missing. Moewes
5 Decl., ¶ 22, Ex. 15. Ms. Moewes requested the signature page
6 in an email on November 14, 2006 and additional documents in an
7 email on November 15, 2007. Moewes Decl., Exs. 16, 17, 18. In
8 the last email, Ms. Moewes threatened to file a motion to
9 compel discovery responses if the relevant documents were not
10 produced. Finally, on November 17, 2006, Mr. Araki sent
11 Ms. Moewes the complete Lake Front buying partner agreement
12 with the signature page indicating it had been signed by
13 Mr. Kenny North. This was the first time the Trustee learned
14 of the involvement of Kenny North in the Laning transaction.
15 Moewes Decl., ¶¶ 28, 29. This new information came only four
16 days before the Trustee's response to the First Motion for
17 Summary Judgment was due and three weeks after the answers to
18 the First Requests were due.

19 With the assistance of Herman Recor, Michael Levenhagen
20 filed a nine-page declaration in support of the First Motion
21 for Summary Judgment. See Declaration of Michael Levenhagen
22 filed October 13, 2005, Docket no. 37 ("First Levenhagen
23 Decl."). In that declaration, Mr. Levenhagen testified that
24 GFS initially contacted him through a person named Rob Gallert.
25 *Id.* at ¶ 3. Mr. Levenhagen believed that the GFS program
26 involved helping distressed homeowners remain in their homes
and investing in property for a fee. Mr. Levenhagen contended

1 that he and his wife were good faith purchasers of the 11609
2 Property for value and were without knowledge that the Debtors
3 were the sellers of the property until after the closing of the
4 sale. Mr. Levenhagen further testified that his communications
5 with Mr. Simonson occurred only after closing in an effort to
6 resolve his concerns about the transaction and that he believed
7 the Debtors were also victims of GFS and David Langford.
8 Mr. Levenhagen described his transactions with Network and how,
9 in December of 2005, Mark Laing purchased the 11609 Property
10 and paid off the loans the Levenhagens had obtained to finance
11 their purchase of the 11609 Property. Sixty seven pages of
12 documents were attached to the First Levenhagen Declaration -
13 the SBA, however, was not included among those documents nor
14 was any correspondence or emails between the Levenhagens and
15 the Debtors.

16 In the Debtors' Summary Judgment Motion the Debtors
17 asserted:

18 The undisputed evidence shows that the Defendants
19 Doug and Karen Simonson should be dismissed from
20 the present litigation as they had nothing to do
21 with the fraud against the banks or any other
22 person in connection with the properties. The
23 proper claims to be pursued are those against
24 Global Financial Solutions, Mr. Dave Langford,
25 Mark Hodges & Associates and Kevin Magorien as
26 these are the parties who enabled the fraud to
occur with respect to the properties and the
resultant harm or damage to the creditors and/or
the banks. The evidence is irrefutable that Doug
and Karen Simonson received NO money from the
sale of the properties to GFS.

Debtors' Summary Judgment Motion, 10/24/06 (Docket no. 50).

The Trustee objected to the First Motion For Summary

1 Judgment (Docket no. 61) and to the Debtors' Summary Judgment
2 Motion (Docket no. 63) contending that, notwithstanding the
3 assertions by the Levenhagens and the Debtors that they were
4 innocent victims of a scheme by GFS, the Debtors were the
5 ultimate beneficiaries of "these schemes...to get the [11609
6 Property] and lot back into the Simonson's name, or under their
7 control, after having successfully 'washed' the properties
8 through these many transfers, and providing tranches of cash to
9 the Simonsons at several points along the way." Trustee's
10 Response to First Motion for Summary Judgment, pp. 1, 2. The
11 Trustee further contended that Mr. Simonson was the architect
12 of the buying partner program and a direct participant in GFS.

13 Beginning on page 6 of the Trustee's response, the Trustee
14 described the shortcomings in the document production made by
15 the Transferee Defendants. Included with the documents filed
16 by the Trustee in support of his response were (i) a copy of
17 the Daniels Capital deed of trust against the 11609 Property
18 showing Network (by Mr. Simonson) as the grantor, Daniels
19 Capital as the grantee, and Herman Recor as the trustee, (ii) a
20 copy of the General Buying Partner Agreement, and (iii) a copy
21 of the SBA. Declaration of Denice Moewes in Support of
22 Trustee's Response to Motion for Summary Judgment, Docket no.
23 62 ("11/21/06 Moewes Decl."), Ex. 4. The Trustee's copy of the
24 General Buying Partner Agreement, which he had obtained in
25 discovery from Mr. Simonson, differed from the one
26 Mr. Levenhagen had sent to Herman Recor in that there was no
reference to "Doug Simonson" on the GFS signature line.

1 Compare Ex. 4, 11/21/06 Moewes Decl., to Ex. 12, Levenhagen
2 Decl. The Trustee contended that the Levenhagens were not in
3 good faith and that they were liable as transferees of the
4 11609 Property under Section 550 of the Bankruptcy Code.

5 At the hearing on December 1, 2006, the Court orally denied
6 the First Motion for Summary Judgment, ruling that: (a) the
7 Levenhagens were the initial transferees under
8 Section 550(a)(1) of the 11609 Property; (b) the Laings were
9 the initial transferees under Section 550(a)(1) of Network; and
10 (c) the Lanings were the immediate or mediate transferees of
11 the 11611 Property. The order on this ruling was not entered
12 until January 24, 2007 (Docket no. 115). In addition, the
13 Court orally denied the Debtors' Summary Judgment Motion.

14 At the hearing on December 1, the Court warned the parties
15 that due to statements in a number of the declarations which
16 described possible criminal activities, the Court was required
17 to refer the case to the U.S. Attorney's Office for criminal
18 investigation. The Court also noted on the record because that
19 Herman Recor appeared as the trustee on the Daniels Capital
20 deed of trust and on other documents, Herman Recor attorneys
21 might be considered fact witnesses in the case. The Court
22 instructed counsel for the Trustee to make an early
23 determination of whether she would seek to depose Mr. Araki or
24 other attorneys at Herman Recor so as not to prejudice the
25 Transferee Defendants by waiting until the trial to deal with
26 these issues.

Eleven days after the Court orally denied the First Motion

1 for Summary Judgment, the Transferee Defendants filed three new
2 motions for summary judgment, one challenging the Court's
3 jurisdiction, one seeking dismissal of the Trustee's claim to
4 vacate the Abandonment Order, and one requesting dismissal of
5 all claims against Sylvia Laing and Nancy Laning (collectively,
6 the "Second Summary Judgment Motions"). These motions were set
7 for hearing on January 5, 2007. On December 15, 2006, the
8 Trustee filed a motion for summary judgment requesting the
9 Court to vacate the Order of Abandonment under Rule 60(b),
10 Fed.R.Civ.P., on the ground that the order had been entered as
11 a result of a fraud upon the Court (the "Trustee's Summary
12 Judgment Motion"). This motion was set for hearing on
13 January 19, 2007.

14 The Trustee served his second request for production of
15 documents on the Transferee Defendants on December 7, 2006.
16 These requests sought production of the Transferee Defendants'
17 tax returns, which were produced as requested. On February 24,
18 2007, the Trustee served on Herman Recor third requests for
19 production of documents against each of the Transferee
20 Defendants (collectively, the "Third Requests"). Responses to
21 the Third Requests were due on March 26, 2007. Included in the
22 Third Requests to the Levenhagens was Request for Production
23 No. 3, which stated:

24 Please produce any and all correspondence,
25 including emails, phone messages, letters or
26 other communication documents between 1) the
Levenhagens and the debtors; 2) the Levenhagens
and the debtors' attorneys; 3) the Levenhagens
and any other defendants to this proceeding; 4)
the Levenhagens and any other defendant's legal

1 counsel; 5) the Levenhagens or any entity acting
2 on their behalf and any entity other than their
3 counsel which relate to or mention this
4 proceeding, the subject matter of this
5 proceeding, any defendants named in this
6 proceeding, the debtors, the debtors counsel, and
7 the property which is referenced in the
8 Complaint.

9 The quoted request repeated the request contained in the
10 Levenhagen Requests for emails between the Debtors and the
11 Levenhagens. Request for Production No. 4 sought production of
12 correspondence, including emails, between the Levenhagens and
13 Kenny North.

14 On January 5, 2007, the Court denied the Second Summary
15 Judgment Motions and on January 17, 2007, the Court granted the
16 Trustee's Motion for Summary Judgment. In connection with the
17 Trustee's motion, the Trustee produced documents evidencing
18 that Mr. Simonson was owed substantial commissions for his work
19 for GFS, including over \$100,000 in commissions from the sale
20 of his own properties.³ See Declaration of Denice Moewes in
21 Support of Trustee's Motion for Summary Judgment on Trustee's
22 Complaint Asking Court to Vacate its Order Abandoning Property
23 of the Estate (Docket No. 81), Exs. 12, 13. The Court also
24 held that the Abandonment Order should be vacated pursuant to
25 Rule 60(b), Fed.R.Civ.P., on the ground that it was procured by
26 a fraud on the Court. An order to that effect was approved by
27 the Court and docketed on February 13, 2007 (Docket no. 128).

3

28 This evidence contradicted the assertions of the
29 Levenhagens in the First Motion for Summary Judgment that the
30 Debtors were just victims of GFS and had no financial
31 arrangements with GFS.

MEMORANDUM DECISION - 18

1 On the same date, the Court entered an order setting a trial
2 date of May 8, 2007.

3 In March of 2007 the Trustee was able to reach an agreement
4 with Herman Recor on the timing and location of the Trustee's
5 depositions of the Levenhagens and the Lanings. The Trustee
6 therefore noted the depositions of the Levenhagens for April 2,
7 2007 in Minneapolis, Minnesota, and the Lanings for April 3,
8 2007 in Chicago, Illinois. Moewes Decl., ¶ 32, Ex. 21.
9 Counsel for the Trustee was anticipating receipt of the
10 documents responsive to the Third Requests on Monday, March 26,
11 2007, in time to review them and have them available for the
12 depositions by the first week of April. Despite the fact that
13 Herman Recor had in its possession as of March 26, 2007
14 documents responsive to the Third Requests which had not yet
15 been turned over to the Trustee, and despite the Trustee's
16 request for responses again on March 26, 2007, additional
17 documents were not made available to Trustee's counsel until
18 4:30 pm. on Wednesday, March 28, 2007. In Ms. Moewes'
19 judgment, this was too late for meaningful review and delivery
20 out-of-state for the depositions. Moewes Decl., ¶40.

21 The March 28 production of documents by Herman Recor did
22 include 88 emails and fax documents which Mr. Levenhagen had
23 produced as part of the November 1 2006 Documents, but none of
24 these documents were dated after January 18, 2006. *Id.*, ¶48.
25 The production did *not* include, however, 43 additional emails
26 and faxes which Herman Recor had in its possession. Moewes
Decl., ¶¶41, 42, Ex. 28. Herman Recor made no objections to

1 Requests for Production 3 and 4 referenced above. *Id.*, ¶40.

2 The Trustee's Motion for Summary Judgment against the
3 Levenhagens (Docket no. 183) was filed on March 27, 2007 and
4 noted for hearing on April 20, 2007. Ms. Moewes flew to
5 Minnesota for the Levenhagens' depositions on April 2. At the
6 deposition, Mr. Levenhagen agreed to search for and produce to
7 his counsel responsive documents dated after January 18, 2006.
8 The deposition was aborted, however, because Herman Recor had
9 advised Mrs. Levenhagen that she did not need to appear at the
10 deposition, despite the fact that the notice of deposition
11 required her appearance. Further, when Mr. Levenhagen learned
12 at the deposition for the first time that the Court had
13 referred the whole proceeding for criminal investigation he
14 wanted an opportunity to consult with criminal counsel before
15 continuing the deposition. Herman Recor had not advised the
16 Levenhagens of the criminal referral the Court advised it was
17 required to make at the December 1, 2006 hearing. Moewes
18 Decl., Ex. 21.

19 After the aborted depositions, Ms. Moewes reminded
20 Mr. Araki in an April 13, 2007 email of Mr. Levenhagen's
21 commitment at the deposition to produce emails dated after
22 January 18, 2006. Mr. Araki never responded to this email
23 despite the fact that he had received responsive documents from
24 Mr. Levenhagen on both March 2, 2007 and April 4, 2007.
25 Levenhagen Decl., ¶¶19, 21, 22, 23, Exs. 7, 8.

26 The Trustee's Third Amended Complaint was filed on
April 18, 2007 (Docket no. 203). The Third Amended Complaint
MEMORANDUM DECISION - 20

1 added Lake Front and New Century as defendants. The complaint
2 alleged that on October 11, 2005, the Laings had entered into a
3 Buying Partner General Terms of Agreement with New Century and
4 a Specific Buying Partner Agreement with New Century pursuant
5 to which they would finance the purchase of the 11609 Property
6 as the nominees for New Century. The Trustee alleged that the
7 Buying Partner General Terms of Agreement was signed by Kenny
8 North as President of New Century and that the purchase price
9 for the 11609 Property was to be no more than \$1,650,000. The
10 Third Amended Complaint contained new allegations that David
11 Laning entered into a Buying Partner General Terms of Agreement
12 and a Specific Buying Partner Agreement with Lake Front
13 pursuant to which Laning would act as Lake Front's nominee in
14 purchasing the 11619 Property for no more than \$1,300,000.

15 On April 20, 2007, the Court granted the Trustee's Motion
16 for Summary Judgment against the Levenhagens, rejecting the
17 Levenhagens' continued assertion in pleadings filed by Herman
18 Recor that they were good faith purchasers of the 11609
19 Property without knowledge of the involvement of the Debtors
20 until after the sale occurred. The Court also ordered the
21 parties to attend a settlement conference and attempt to agree
22 on a form of remedy for the Trustee and the estate in light of
23 the Court's finding that the Levenhagens were strictly liable
24 as initial transferees under Bankruptcy Code § 550.

25 One month later, on May 15, 2007, Mr. Araki advised
26 Ms. Moewes by email that he was in the process of drafting an
email to his clients advising them that "I believe there is a

MEMORANDUM DECISION - 21

1 real possibility now for a conflict of interest on the part of
2 our firm and that we will be filing our motion to withdraw."
3 Moewes Decl., Ex. 28. On June 8, 2007, Herman Recor withdrew
4 as counsel for the Transferee Defendants and Mr. Marc Stern
5 substituted in as their counsel.

6 When Ms. Moewes finally took Mr. Levenhagen's deposition on
7 October 31, 2007, with the assistance of Mr. Stern,
8 Mr. Levenhagen testified about the emails and other documents
9 he had delivered to Herman Recor. After the deposition,
10 Mr. Stern made the documents Mr. Levenhagen had produced to
11 Herman Recor available to Ms. Moewes. In the process of
12 examining those documents Ms. Moewes found all of the documents
13 that Herman Recor had either not timely produced in response to
14 the Trustee's discovery requests or had not produced at all.
15 The Trustee has assembled the emails and fax documents that
16 were in the records from Herman Recor clipped together with a
17 yellow cover sheet identifying them as "emails btwn
18 Levenhagen/Simonson" in Exhibit 35 to the Moewes Decl.
19 Exhibit 45 to the Moewes Decl. contains all of the emails and
20 faxes Herman Recor never turned over to the Trustee.

21 C. The Trustee's Motion for Sanctions.

22 The Trustee's Memorandum in Support of Trustee's Motion for
23 Sanctions Against Herman Recor Araki Kaufman Simmerly &
24 Jackson, PLLC For Violations of Discovery Rules describes in
25 detail, beginning at page 46 and continuing to page 52, each of
26 Herman Recor's alleged violations of the discovery rules at
issue. These violations include falsely representing that all

1 responsive documents had been produced (when they clearly had
2 not been), failing to provide discovery responses in a timely
3 fashion, substantially delaying the release of responsive
4 documents even after repeated requests for supplementation were
5 made by the Trustee, producing incomplete and/or altered
6 documents (Moewes Decl., ¶43, Ex. 29), and failing completely
7 to produce substantial relevant documents. For these discovery
8 abuses, the Trustee seeks compensatory damages of \$136,864.93
9 plus attorneys' fees and costs incurred in bringing the
10 Sanctions Motion of \$95,174.50.

11 In response to the Sanctions Motion, Herman Recor did not
12 deny its failure to produce documents relevant and responsive
13 to the Trustee's discovery requests. Instead, Herman Recor
14 argued that any failures on its part were unintentional and not
15 prejudicial to the Trustee or his position in the litigation.
16 Mr. Robert Jackson filed a declaration in opposition to the
17 Sanctions Motion in which he testified that he had no specific
18 recollection of the emails that were part of the Withheld
19 Documents, that he was not involved in any deliberate
20 withholding of any documents, and that his normal practice was
21 to forward documents and emails to Leanne Volz, Herman Recor's
22 litigation paralegal. Declaration of Robert B. Jackson in
23 Opposition to Trustee's Motion for Sanctions for Violations of
24 Discovery Rules, Docket no. 352. Mr. Jackson speculated that
25 because he was "organizing and reorganizing" emails in the
26 process of preparing responses to the Trustee's discovery
requests, he may have "excluded e-mails to assess whether they
MEMORANDUM DECISION - 23

1 were privileged." *Id.* His declaration describes his
2 involvement with GFS, the Debtors, the Levenhagens and Kenny
3 North. Mr. Araki also filed a declaration in opposition to the
4 Sanctions Motion. In his declaration, Mr. Araki testified that
5 he did not participate extensively in the discovery requests
6 and therefore could not recall the exact details of the
7 process. Declaration of Stephen T. Araki in Opposition to
8 Trustee's Motion for Sanctions for Violations of Discovery
9 Rules, Docket no. 353. He did admit that he received emails
10 from the Levenhagens and that it was his custom to forward
11 those to Ms. Volz. Like Mr. Jackson, Mr. Araki claimed not to
12 have any specific recollection of the emails in the Withheld
13 Documents but attested that he was not involved in any
14 deliberate withholding of documents. Ms. Volz filed her own
15 declaration in opposition to the Sanctions Motion in which she
16 testified that she was receiving documents from the Transferee
17 Defendants on an almost daily basis and that she reviewed and
18 copied them for production. Declaration of Leanne Volz in
19 Opposition to Trustee's Motion for Sanctions for Violations of
20 Discovery Rules, Docket no. 354. She stated that she believed
21 she had sent all responsive documents to the Trustee and at no
22 time ever redacted or was instructed to redact documents from
23 Mr. Levenhagen. In sum, Herman Recor provides no explanation
24 or justification for the failure to produce the Withheld
25 Documents or for alternations to certain of the documents.

26 At the hearing on the Sanctions Motion on July 11, 2008,
the Court orally ruled that Herman Recor had not demonstrated

1 that its failure to timely and completely respond to the
2 Trustee's discovery requests was substantially justified and
3 that an award of compensatory damages to the Trustee would not
4 be unjust. The Court took the amount of compensatory damages
5 to be awarded under advisement and asked the parties to provide
6 supplemental materials on that question. The Court also noted
7 that punitive or non-compensatory damages would not be awarded
8 in the absence of an evidentiary hearing.

9 III. DISCUSSION

10 This case presents the most serious allegation of discovery
11 misconduct the Court has encountered. When parties or their
12 lawyers determine, independently of the rules of civil
13 procedure, what should or should not be produced to their
14 opponent, the adversary system breaks down. Thus, the
15 importance of enforcing the rules of discovery, which are
16 intended to put different sides in litigation on the same
17 plane, cannot be overstated. *See United Medical Supply Co. v.*
18 *U.S.*, 77 Fed.Cl. 257, 258-59 (Fed.Cl. 2007) ("Aside perhaps from
19 perjury, no act serves to threaten the integrity of the
20 judicial process more than the spoliation of evidence. Our
21 adversarial process is designed to tolerate human failings -
22 erring judges can be reversed, uncooperative counsel can be
23 shepherded, and recalcitrant witnesses compelled to testify.
24 But, when critical documents go missing, judges and litigants
25 alike descend into a world of *ad hocery* and half measures-and
26 our civil justice system suffers.").

In this case, the evidence Herman Recor withheld from the
MEMORANDUM DECISION - 25

1 Trustee was discovered only after Herman Recor withdrew from
2 its representation of the Transferee Defendants and another
3 attorney was retained by the Levenhagens. No effort was ever
4 made by Herman Recor to correct its failure to produce
5 documents or to supplement discovery requests with documents it
6 withheld.

7 A. The Court's Inherent Power to Impose Sanctions.

8 The Court has both inherent and statutory power to impose
9 discovery sanctions. In *Chambers v. NACSO, Inc.*, 501 U.S. 32,
10 45-46, 111 S.Ct. 2123 (1991), the Supreme Court recognized the
11 inherent power of courts to impose appropriate sanctions where
12 conduct disrupts the judicial process. This inherent power
13 resides in the bankruptcy court. In *re Rainbow Magazine, Inc.*,
14 77 F.3d 278 (9th Cir. 1996). The Ninth Circuit has held that
15 sanctions are available under the court's inherent power if
16 "preceded by a finding of bad faith, or conduct tantamount to
17 bad faith," such as recklessness "combined with an additional
18 factor such as frivolousness, harassment, or an improper
19 purpose." See *Fink v. Gomez*, 239 F.3d 989, 994 (9th Cir. 2001);
20 see also *Gomez v. Vernon*, 255 F.3d 1118, 1134 (9th Cir. 2001).

21 B. The Court's Statutory Power to Impose Sanctions.

22 The Court's statutory power to impose sanctions arises
23 under Rule 26 and Rule 37, Fed.R.Civ.P. Sanctions for
24 violation of Rule 37 may be imposed for negligent conduct. See
25 Fed.R.Civ. P. 37(b); *Fjelstad v. American Honda Motor Co.*,
26 *Inc.*, 762 F.2d 1334, 1343 (9th Cir. 1985); *Hyde & Drath v.*
Baker, 24 F.3d 1162, 1171 (9th Cir. 1994) ("We have not required

1 a finding of bad faith on the part of the attorney before
2 imposing sanctions under Rule 37."). The lack of bad faith
3 does not immunize a party or its attorney from sanctions,
4 although a finding of good or bad faith may be a consideration
5 in determining whether imposition of sanctions would be unjust,
6 see *Hyde & Drath*, 24 F.3d at 1171, and the severity of the
7 sanctions. Only the most drastic sanction, dismissal,
8 generally requires a finding that the conduct was "due to
9 willfulness, bad faith or fault of the party...." *In re*
10 *Phenylpropanolamine (PPA) Products Liability Litig.*, 460 F.3d
11 1217, 1233 (9th Cir.2006). Importantly, "[b]elated compliance
12 with discovery orders does not preclude the imposition of
13 sanctions." See *North American Watch Corp. v. Princess Ermine*
14 *Jewels*, 786 F.2d 1447, 1451 (9th Cir. 1986); see also *G-K*
15 *Properties v. Redevelopment Agency of City of San Jose*, 577
16 F.2d 645, 647-48 (9th Cir.1978).

17 In this case, both subsections (c) and (d) of Rule 37
18 apply. Subsection (c) permits the Court to order "payment of
19 the reasonable expenses, including attorney's fees, caused by"
20 a party's failure to provide information as required by
21 Rule 26(a) or (e) "unless the failure was substantially
22 justified or is harmless." Rule 26(a), responses to requests
23 for production of documents, and 26(e), supplementing those
24 responses, are implicated here by Herman Recor's conduct.

25 Rule 37(d)(3) mandates the Court to "require the party
26 failing to act, the attorney advising that party, or both to
pay the reasonable expenses, including attorney's fees, caused

1 by the failure unless the failure was substantially justified
2 or other circumstances make an award of expenses unjust." The
3 failures for which sanctions are authorized under Rule 37(d)
4 include under (1)(A)(i) a party's failure to attend a
5 deposition, or under (ii) failure to respond to a request under
6 Rule 34, which covers the disclosure of electronically stored
7 information. Rule 37(d)(2) specifically provides that failure
8 to produce requested discovery on the ground that the discovery
9 sought was objectionable, is not an acceptable excuse for
10 failing to produce the discovery.

11 Finally, Rule 26(g), Fed.R.Civ.P., requires that each
12 disclosure be signed by at least one attorney of record and by
13 signing, that attorney certifies that to the best of their
14 knowledge, information and belief "formed after a reasonable
15 inquiry" each disclosure is complete and correct as of the time
16 it is made, and that as to responses to discovery requests, the
17 response is not interposed for any improper purpose such as to
18 cause unnecessary delay or needlessly increase the cost of
19 litigation. Rule 26(g)(3) states that if a certification
20 violates this rule "without substantial justification" the
21 court "must impose" an appropriate sanction on the signer, the
22 party on whose behalf the signer was acting, or both. The
23 sanction may include an order to pay the reasonable expenses,
24 including attorney's fees, caused by the violation.

25 Although federal law and the Federal Rules of Civil
26 Procedure apply to this case, a Washington Supreme Court
decision, *Washington State Physicians Insurance Exchange &*

1 *Association v. Fisons Corp.*, 122 Wash.2d 299, 858 P.2d 1054
2 (1993), provides additional guidance as to how the above
3 described rules should be applied. In addressing whether the
4 lower court should have awarded sanctions against a drug
5 company for discovery abuse, the court held that the inherent
6 power of the court to sanction should not be used where other
7 court rules more properly apply. The court further held that
8 the sanction provision of Washington Civil Rule 37 should not
9 be applied where the more specific provisions of Rule 26 better
10 fit the situation. The court went on to construe Washington
11 Civil Rule 26(g), which is virtually identical to Rule 26(g),
12 Fed.R.Civ.P., looking to federal law for guidance. The court
13 concluded after reviewing federal authorities that
14 "[s]ubjective belief or good faith alone no longer shields an
15 attorney from sanctions under the rules," that intent need not
16 be shown before sanctions are mandated, and a motion to compel
17 compliance with the rules is not a prerequisite to a sanctions
18 motion. *Id.* at 1078. The court held that in determining
19 whether an attorney has complied with the rule, the trial court
20 should consider all of the surrounding circumstances, the
21 importance of the evidence to its proponent, and the ability of
22 the opposing party to formulate a response or comply with the
23 request.

24 C. The Trustee's Right to Compensation Under Rule 26(g).

25 Rule 26(g), Fed.R.Civ.P., applies to the circumstances at
26 issue in this case. Thus, there is no need for the Court to
utilize Rule 37 or its inherent powers to issue sanctions.

1 Having found that Herman Recor was not substantially justified
2 in failing to provide discovery to the Trustee, Rule 26(g)
3 requires the Court to award sanctions to the Trustee, including
4 reasonable attorneys' fees caused by the violation.

5 It should be noted that the Trustee has not sought any
6 sanctions against the Levenhagens. Mr. Levenhagen produced
7 documents promptly and completely. If anything, the
8 Levenhagens were cast in an uncooperative and negative light by
9 their counsel's failure to turn over documents to the Trustee.

10 1. Consideration of the Surrounding Circumstances.

11 On October 13, 2006, when Herman Recor filed the First
12 Motion for Summary Judgment on behalf of the Transferee
13 Defendants, it had the Withheld Documents in its possession,
14 including 119 emails and faxes. These documents should have
15 been produced by October 27, 2006, in advance of the hearing on
16 the First Motion for Summary Judgment, which was set for
17 November 3, 2006. When the hearing finally took place on
18 December 1, 2006, after being continued because of Herman
19 Recor's failure to respond to the First Requests, Herman Recor
20 had not produced to the Trustee the Withheld Documents nor
21 advised the Trustee that these documents had not been produced
22 with the First Response on November 7, 2006. As of the time of
23 the hearing on the Second Summary Judgment Motions on
24 January 5, 2007 and the Trustee's Summary Judgment Motion on
25 January 19, 2007, the Withheld Documents had not been produced
26 to the Trustee. It was not until March 28, 2007, that Herman
Recor finally produced 88 emails and faxes from the November 1

1 2006 Documents. At that date, Herman Recor was still
2 withholding an additional 43 emails and faxes that were
3 responsive to the prior production requests of the Trustee.
4 These documents were still being withheld by Herman Recor from
5 the Trustee when Ms. Moewes flew to Minneapolis for the
6 Levenhagens' depositions on April 2, 2007, when the Trustee
7 filed the Third Amended Complaint on April 18, 2007, when the
8 Trustee's Motion for Summary Judgment Against the Levenhagens
9 was heard on April 20, 2007, and when the Trustee took
10 Mr. Levenhagen's deposition on October 31, 2007. Thus, when
11 the Trustee was defending or pursuing the most important pre-
12 trial motions in the case, he was disadvantaged by Herman
13 Recor's untimely disclosures and nondisclosures. Six of the
14 motions the Trustee was forced to defend during this time
15 period were brought by Herman Recor and four of those motions
16 were heard after answers to the First Requests were due from
17 the Transferee Defendants.

18 The documents withheld by Herman Recor implicated other
19 defendants, which forced the Trustee to amend his Complaint
20 twice. The emails that were withheld showed the significant
21 involvement of Mr. Simonson in the activities of GFS and the
22 involvement of Mr. Jackson and Mr. North in a number of the
23 transactions at issue. The names of attorney Robert Jackson
24 and Kenny North had already come up in related litigation in
25 adversary case number 06-01041 (also assigned to this Court),
26 where the Trustee sued the Debtors for turnover of estate
funds. In that litigation, the Court held that the Debtors had

1 violated a restraining order issued by the Court prohibiting
2 the Debtors from using certain funds. To avoid the Trustee's
3 discovery of the Debtors' circumvention of the restraining
4 order in that case, the Simonsons had borrowed money from Kenny
5 North, deposited the funds into Mr. Jackson's trust account,
6 then accessed the money by having Mr. Jackson issue cashier's
7 checks to Mr. Simonson which could not be traced by the
8 Trustee. After a trial concluding on April 26, 2006, the Court
9 issued a letter ruling on May 10, 2006 finding the Debtors in
10 contempt and ordering Mr. Jackson to turn over to the Trustee
11 any funds of the Debtors paid to him after the issuance of the
12 restraining order. The Court ultimately denied the Debtors'
13 discharge based upon their conduct. See Case No. 06-01041,
14 Docket nos. 169, 144.

15 The emails Herman Recor withheld from the Trustee in
16 discovery in this adversary proceeding provide further evidence
17 of Mr. Jackson's involvement in numerous other transactions
18 related to the Simonsons as well as the involvement of Kenny
19 North and his companies, Lake Front and New Century. The
20 Withheld Documents include documents relevant to the
21 transactions between the Debtors, the Levenhagens, and Network
22 and the deed of trust transaction between Network and Daniels
23 Capital, which Mr. Levenhagen did not know about until after
24 Herman Recor withdrew from representing him. Levenhagen Decl.,
25 ¶¶ 29, 30, 36, 40. In addition, Mr. Levenhagen did not know
26 that Mr. Araki was the escrow agent for the Daniels Capital
transaction and that Herman Recor was the trustee under the

1 Daniels Capital deed of trust. *Id.*, ¶36. Mr. Levenhagen did
2 not know where the \$167,775 in Daniels Capital loan proceeds
3 went until the Trustee discovered the funds were deposited into
4 Herman Recor's trust account and then paid to Network. Moewes
5 Decl., Exs. 38, 39. Nevertheless, the Daniels Capital deed of
6 trust represented an increase in the debt secured by the 11609
7 Property which the Levenhagens' believed they owned.

8 Herman Recor's discovery abuses delayed the trial,
9 complicated the case, and significantly increased the costs to
10 the Trustee. Because bankruptcy trustees must use funds of the
11 estate to compensate their lawyers, every dollar spent on
12 litigation costs is a dollar that does not reach the pockets of
13 the debtor's creditors. Thus, increased costs in bankruptcy
14 litigation force trustees to accept settlements a fully funded
15 litigant might not otherwise accept or force trustees to limit
16 litigation activities to their disadvantage. The billing
17 statements provided by Wood & Jones, counsel for the Trustee,
18 evidence the significant expense incurred by the Trustee in
19 this litigation.

20 2. The Importance of the Discovery to the Trustee.

21 Herman Recor argues that the nondisclosures were harmless
22 because most of the information withheld was ultimately
23 discovered by the Trustee from other sources. First, that is
24 simply not true. The emails between Mr. Levenhagen and the
25 Debtors and other defendants would not have been and were not
26 discovered from other sources. Second, even if some of the
documents were ultimately discovered by the Trustee, it was

1 only after an expensive discovery and summary judgment process.
2 The Trustee fought off a total of four different motions
3 brought by Herman Recor on behalf of the Transferee Defendants
4 while Herman Recor withheld documents relevant to those
5 motions.

6 The Trustee contends that the Withheld Documents would have
7 provided support for the Trustee's contention that Mr. Simonson
8 was working for GFS and was not another victim of GFS as
9 Mr. Levenhagen contended in support of the First Motion for
10 Summary Judgment. Herman Recor responds that the Trustee
11 already had information to suggest Mr. Simonson's direct
12 involvement with GFS by November of 2006 when the Trustee filed
13 his response to the Transferee Defendants' First Motion for
14 Summary Judgment and that therefore the Trustee was not
15 prejudiced in any way. This argument, however, points out just
16 how fortuitous it was that the Trustee had obtained some
17 evidence of Mr. Simonson's involvement with GFS because the
18 First Motion for Summary Judgment drafted by Herman Recor made
19 the argument that Mr. Simonson was just another victim of a
20 scheme by GFS and Dave Langford. In fact, the First Motion for
21 Summary Judgment in footnote 8 states that "Mr. Simonson did
22 not benefit from the sale to these third parties, nor did he
23 have any financial arrangement or agreement with Global
24 Financial Solutions." That statement was clearly false. In a
25 March 17, 2005 email from Doug Simonson to Tiffany Doty (who
26 appears to have been an associate of David Langford),
Mr. Simonson complained that he had "worked his heart out"

1 producing buying partners for 30 GFS deals for which he should
2 have been paid commissions by GFS of over \$200,000. Moewes
3 Decl., Ex. 45, p. 26. He further describes how GFS failed to
4 pay his business expenses for the company. *Id.* Other emails
5 from Mr. Simonson indicated his use of a GFS email account,
6 i.e. doug.simonson@fg-solutions.com. *Id.* at p. 8. None of
7 these emails had been produced to the Trustee by the time the
8 Trustee was required to respond to the First Motion for Summary
9 Judgment.

10 Also included with the Withheld Documents is a March 6,
11 2006 email from Mr. Simonson to Mr. Levenhagen in which
12 Mr. Simonson essentially coaches Mr. Levenhagen as to how to
13 describe the transactions related to the 11609 Property in the
14 event Mr. Levenhagen's subpoena to testify is not quashed. The
15 email reads in part: "Hi Mike, I believe we will get your
16 subpoena dropped. But, in case we do not I wanted to give you
17 some background and refresh your memory a bit on this whole
18 thing." *Id.*, p. 100. Following that introductory statement,
19 Mr. Simonson's email proceeds as a lengthy and detailed
20 description of how he sees the transactions and the litigation.
21 The Trustee would have been better able to judge the
22 credibility of both Mr. Levenhagen and Mr. Simonson had he had
23 access to the contents of this email. The email appears not to
24 have been provided to Herman Recor by Mr. Levenhagen until
25 April 4, 2007, however, only because Mr. Levenhagen was under
26 the misunderstanding that he did not have to produce email
communications after January of 2006. See Second Declaration

1 of Cynthia A. Kuno, Docket no. 376, Ex. D. Had Herman Recor
2 done its job, Mr. Levenhagen would have been advised that the
3 Levenhagen Request did not limit the time for production to
4 communications prior to that date.

5 Included in the Withheld Documents were the transactional
6 documents reflecting the transfer of Network from the Debtors
7 to the Levenhagens and back. Herman Recor concedes that at the
8 December 1, 2006 hearing, Mr. Wood noted that the Trustee
9 lacked documentation as to that transaction. However, Herman
10 Recor argues that once the Court held on that date that the
11 Levenhagens were the initial transferees for purposes of
12 Section 550, the documents related to the transfers were
13 irrelevant. This ignores the fact, however, that the Trustee
14 would need to follow the interest in Network and in the 11609
15 and 11611 Properties into the hands of Laing and Laning. Thus,
16 the transactional documents related to the Network transaction
17 were relevant to the Trustee's pursuit of these other
18 defendants and should have been produced.

19 The Trustee contends that had the Withheld Documents been
20 produced, he would have understood earlier in the litigation
21 how Kenny North, Lake Front, and New Century were involved in
22 the challenged transactions. Herman Recor argues that by the
23 time the Trustee filed his response to the First Motion for
24 Summary Judgment on November 22, 2006, the Trustee already knew
25 that Kenny North had some involvement. Herman Recor concedes,
26 however, that the Trustee had to acquire this information
through subpoenas of escrow files from Taylor and Associates.

1 The emails contained in Exhibit 45 to the Moewes Decl. contain
2 very detailed information about Kenny North's involvement in
3 the disputed transactions. This information would have been
4 readily available to the Trustee had it been timely produced by
5 Herman Recor. The fact that the Trustee was once again
6 fortuitous enough to have obtained the information elsewhere in
7 time to respond to a summary judgment motion by the Transferee
8 Defendants does not eliminate the prejudice resulting from the
9 wrongful withholding of the information.

10 Finally, the Trustee argues that the Withheld Documents
11 evidenced that attorneys at Herman Recor, in particular Robert
12 Jackson, had significant involvement in the transactions at
13 issue and might be fact witnesses. The fact that the Court
14 pointed out at the hearing on December 1, 2006, that the firm
15 name appeared on the Daniels Capital deed of trust does not
16 absolve Herman Recor from liability. In fact, Herman Recor
17 ultimately withdrew as counsel for the Transferee Defendants
18 citing a conflict for the reason.

19 The Court concludes that the Withheld Documents were
20 relevant and material to the Trustee's case and that the
21 Trustee was prejudiced by not having access to the documents.
22 During the time the documents were not available to the
23 Trustee, the Trustee was engaged in expensive discovery,
24 substantial motion practice, and settlement discussions.

25 3. The Ability of Herman Recor to Comply with the
26 Trustee's Discovery Requests.

Herman Recor clearly had the ability to comply with the

Trustee's discovery requests because the documents had been provided to Herman Recor by Mr. Levenhagen well in advance of when the documents were due to be turned over to the Trustee. Mr. Jackson testified in his declaration that the documents in Exhibit 45 "may have been" set aside because they were privileged and then they forgot later to address them. The Court has reviewed the documents in Exhibit 45, however, and concludes that there is no argument that these documents are or were privileged. Further, even if Herman Recor believed the documents to be privileged, the rules require the assertion of the privilege at the time production is required and the creation of a privilege log. Neither occurred in this case.

D. The Award.

The Trustee seeks compensatory sanctions for Herman Recor's discovery abuses in the amounts shown below broken down by category (see Supplemental Declaration of Denice Moewes in Support of Trustee's Memorandum In Support of Trustee's Motion for Sanctions, Docket no. 368). Each of the stated amounts reflects the Trustee's billed time for a particular matter, as follows:

Discovery:	\$ 44,608.00
First Motion for Summary Judgment:	\$ 32,414.50
Second Summary Judgment Motions:	\$ 7,081.00
Trustee's Summary Judgment Motion:	\$ 25,968.00
Trustee's Summary Judgment vs. Levenhagen:	\$ 25,098.00
Expenses for aborted Levenhagen and Laing deposition on April 2 and 3, 2007:	\$ 1,695.43
Subtotal:	\$136,864.93
Attorneys fees incurred in bringing the Sanctions Motion (through June 30, 2008):	\$ 95,174.50
Total:	\$232,039.43

1 Subsequent to the July 11, 2008 hearing, Herman Recor filed
2 a detailed analysis of the Trustee's charges, which categorizes
3 the Trustee's attorneys' billed time into the following three
4 categories: (i) category "N", which includes the charges Herman
5 Recor disputes and contends are not related to its failure to
6 produce discovery, (ii) category "Q", which includes charges
7 Herman Recor asserts are too vague for it to make a
8 determination as to whether the charges arise or are related to
9 its production failure, and (iii) category "R", which includes
10 charges Herman Recor agrees are reasonably related to its
11 failure to timely produce discovery. See Declaration of
12 Cynthia Kuno In Support of Herman Recor Araki Kaufman Simmerly
13 & Jackson PLLC's Memorandum Regarding Trustee's Reasonable Fees
14 Related to Discovery Omissions, Ex. A (Docket no. 375). The
15 fee amounts associated with the charges in the three categories
16 are as follows:

17 Category N (disputed):	\$144,092.00
18 Category Q (vague):	\$105,505.50
19 Category R (reasonably related):	<u>\$ 88,602.50</u>
20 Total:	\$338,200.00

21 Based on the analysis, Herman Recor agrees that \$88,602.50 of
22 the fees sought appear to be related to the discovery abuses,
23 but Herman Recor disputes that the amount of these fees is
24 reasonable. Unfortunately, however, not much more can be
25 gleaned from Herman Recor's analysis. As explained in the
26 letter to the Court from Crocker Kuno dated September 12, 2008
(Docket no. 382), Herman Recor's analysis included *all* of the
Trustee's attorneys' services in this adversary proceeding, not

1 just the fees requested by the Trustee in the Sanctions Motion.
2 Therefore, Crocker Kuno categories N and Q necessarily contain
3 charges for which the Trustee has not sought compensation from
4 Herman Recor.

5 The Court has engaged in a detailed review of the charges
6 sought by the Trustee in the Sanctions Motion as well as the
7 detailed analysis provided by Crocker Kuno. In addition, the
8 Court has reviewed each of the disputed time entries cited by
9 Crocker Kuno at pages 13 through 16 of the Memorandum of Herman
10 Recor Araki Kaufman Simmerly & Jackson PLLC Regarding Trustee's
11 Reasonable Fees Related to Discovery Omissions (the "Herman
12 Recor Memorandum"). The Court will address the specific
13 charges in the Trustee's demand by category. In accordance
14 with the Court's local rules, Wood & Jones has recorded its
15 time for its work in the Main Case into 20 separate categories,
16 including a separate category for this adversary proceeding.
17 Time billed to this adversary proceeding is further broken down
18 into 10 additional categories. See Second Interim Application
19 for Compensation for Reimbursement of Expenses by Wood & Jones,
20 P.S., Attorney for Chapter 7 Trustee filed May 30, 2007 (the
21 "Trustee's Second Application," Docket no. 155); Third Interim
22 Application for Compensation for Reimbursement of Expenses by
23 Wood & Jones, P.S., Attorney for Chapter 7 Trustee filed May 6,
24 2008 (the Trustee's Third Application," Docket no. 222). The
25 Wood & Jones billing statements reviewed by the Court are
26 attached to the Declaration of Denice Moewes In Support of
Second Interim Application for Compensation and Reimbursement

1 of Expenses of Wood & Jones, P.S. Attorney For Trustee and the
2 Declaration of Denice Moewes In Support of Third Interim
3 Application for Compensation and Reimbursement of Expenses of
4 Wood & Jones, P.S. Attorney For Trustee (collectively, the
5 "Moewes Fee App. Declarations")

6 1. Discovery.

7 The Trustee seeks compensation for services performed by
8 his counsel in the amount of \$44,608 related to discovery
9 matters. This amount includes only services performed by Wood
10 & Jones related to discovery after the Transferee Defendants'
11 answers to the First Requests were due on October 27, 2006.
12 See Supplemental Declaration of Denice Moewes in Support of
13 Trustee's Memorandum In Support of Trustee's Motion for
14 Sanctions (Docket no. 368). For the most part, the services
15 for which the Trustee seeks compensation under this category
16 are included in the Trustee's Second Application for Fees.
17 Additional fees related to discovery involving the Transferee
18 Defendants, however, are included in the Trustee's Third
19 Application. The Court has reviewed each of the charges in
20 this category for which the Trustee seeks compensation and
21 concludes that \$28,225.50 in fees are reasonably related to
22 Herman Recor's discovery abuses. The specific charges included
23 by the Court are shown on Exhibit A attached hereto. In a few
24 instances, time entries were lumped and the Court made a
25 reduction in the charge to adjust for time not related to the
26 discovery abuses. In addition, the Court included time
incurred in connection with the second deposition of

1 Mr. Levenhagen which, had the discovery abuses not occurred,
2 would not have been necessary. Herman Recor argues that
3 because the Levenhagens were parties to the action, the Trustee
4 would have had to depose them regardless of the discovery
5 abuses. The problem with that argument is that it ignores the
6 waste of time and expense incurred by the Trustee's attorneys
7 preparing for depositions that had to be aborted and preparing
8 for depositions without all relevant and material documents
9 having been produced in advance of the depositions. Under the
10 circumstances of this case, the Court believes the Trustee
11 should be reimbursed for his attorneys' fees incurred in
12 preparing for and attending both depositions. In making the
13 allowances on Exhibit A in the category of discovery, the Court
14 has taken into account the specific objections at page 13 and
15 14 of the Herman Recor Memorandum.

16 2. First Summary Judgment Motion.

17 The First Motion for Summary Judgment was filed by Herman
18 Recor, was defended by the Trustee, and heard by the Court
19 without the benefit of the Withheld Documents. The Court
20 concludes that Herman Recor should pay Wood & Jones' reasonable
21 attorneys' fees incurred in connection with the motion. The
22 total fees sought under this category are \$32,414.50. The
23 Court holds that all of the requested time is reasonable.
24 Trustee's counsel should have had documents responsive to the
25 First Motion for Summary Judgment well in advance of the
26 December 1, 2006 hearing on the motion. Instead, the First
Response was not made until November 7, 2006 and that

1 production was missing all of the Withheld Documents. Herman
2 Recor argues that because the Trustee prevailed on this motion,
3 he should not be awarded compensation. The Trustee was at a
4 significant disadvantage defending the First Motion for Summary
5 Judgment because of Herman Recor's discovery abuses. The fact
6 that the Trustee was able to piece enough of the relevant
7 transactions together to avoid dismissal of his claims against
8 the Transferee Defendants does not absolve Herman Recor.

9 Within this category of time the Trustee has included
10 charges for legal fees incurred in the Trustee's defense of the
11 Debtor's Summary Judgment Motion. The Court holds that the
12 Trustee should be reimbursed by Herman Recor for these charges
13 as well because the Withheld Documents were directly relevant
14 to Mr. Simonson's claim that he was a mere victim of GFS.
15 Accordingly, the Court will award the Trustee \$32,414.50 in
16 sanctions under this category.

17 3. Second Summary Judgment Motions.

18 In the Second Summary Judgment Motions, the Transferee
19 Defendants raised many of the same factual and legal arguments
20 included in the First Motion for Summary Judgment. The result
21 was the same: the Trustee defended the motions and the Court
22 ruled against the Transferee Defendants. Because the issues
23 were similar to those raised in the First Motion for Summary
24 Judgment, the Trustee incurred only \$7,081 in legal fees under
25 this category for which he seeks reimbursement. For the
26 reasons stated in the preceding section, the Court finds these
fees reasonably related to Herman Recor's discovery abuses and

1 will order that they be reimbursed by Herman Recor.

2 4. Trustee's Motion for Summary Judgment.

3 The Trustee's Summary Judgment Motion sought avoidance of
4 the Abandonment Order under Rule 60(b), Fed.R.Civ.P., on the
5 ground that it had been procured by the fraud of the Debtors in
6 the Main Case. The Trustee seeks reimbursement of \$25,968 in
7 fees related to the motion. There was no allegation in the
8 motion, however, that any of the Transferee Defendants had
9 engaged in any fraud in connection with the entry of the
10 Abandonment Order. Nevertheless, to protect their interests in
11 the 11609 Property and the 11611 Property, the Transferee
12 Defendants filed a response to the Trustee's motion. See
13 Defendant's Response to Trustee's Amended Motion for Summary
14 Judgment filed January 12, 2007, Docket no. 106. The Debtors
15 also opposed the Trustee's motion. See Debtor's Response to
16 Trustee's Amended Motion for summary Judgment filed on
17 January 12, 2007, at Docket no. 108.

18 There is no evidence that any of the Transferee Defendants
19 had anything to do with the procurement of the Abandonment
20 Order in the Main Case. Their transactions with the Debtors
21 occurred after the entry of that order. Although some of the
22 Withheld Documents might have been useful to the Trustee in
23 making the motion under Rule 60(b), the Trustee was able to
24 prevail on the motion without that information. The Court
25 concludes that Herman Recor should not have to reimburse the
26 Trustee for his legal fees incurred in pursuing the Trustee's
Summary Judgment Motion because it was not necessitated by any

1 unlawful conduct of the Transferee Defendants.

2 5. Trustee's Motion for Summary Judgment Against the
3 Levenhagens.

4 The Trustee seeks \$25,098 for reimbursement of his legal
5 fees incurred pursuing the Trustee's Motion for Summary Judgment
6 Against the Levenhagens. In that motion, the Trustee argued
7 that he was entitled to judgment as a matter of law against the
8 Levenhagens as initial transferees of the 11609 Property
9 pursuant to Bankruptcy Code § 550(a)(1). The Court held that
10 it could fashion an equitable remedy under Rule 60(b),
11 Fed.R.Civ.P., after considering all of the facts attendant to
12 the Levenhagens' purchase of the property. The good faith of
13 the Levenhagens was therefore still very much at issue in this
14 motion. In addition, the Levenhagens argued that they were not
15 the initial transferees under Section 550; that GFS was the
16 initial transferee and they were an immediate transferee with
17 the right to assert their good faith as a defense to the
18 Trustee's claims. In their Memorandum the Levenhagens argued
19 that "[i]t was GFS that actually had the right to deal with the
20 property and it is undisputed that GFS directed and controlled
21 the money from the transaction."

22 As of April 2007, when the Court granted the Trustee's
23 Motion for Summary Judgment Against the Levenhagens, the
24 Trustee still was not playing with a full deck of evidence as
25 many of the Withheld Documents had not been produced by Herman
26 Recor. Accordingly, the Court concludes that Herman Recor
should reimburse the Trustee's expenses related to this motion

1 in the amount of \$25,098, which the Court finds reasonable
2 given the significant briefing and factual presentation that
3 was required.

4 6. Out-of-Pocket Expenses for Aborted Depositions.

5 The Trustee seeks reimbursement for out-of-pocket expenses
6 in the amount of \$1,695.43 related to the aborted Levenhagen
7 and Laing depositions on April 2 and April 3, 2007. This
8 amount is reasonable given that the expenses could have been
9 entirely avoided had Herman Recor timely responded to the
10 Trustee's discovery requests and properly advised its clients
11 concerning the depositions.

12 E. The Trustee's Legal Fees Related to the Sanctions
13 Motion.

14 The Trustee requests reimbursement for his fees incurred in
15 bringing the Sanctions Motion. As of July 15, 2008, when
16 Ms. Moewes filed her Supplemental Declaration, these fees
17 totaled \$95,174.50. Herman Recor does not dispute that
18 reasonable fees may be awarded to the Trustee pursuant to Rule
19 26(g)(3), Fed.R.Civ.P., but argues that the fees the Trustee
20 seeks are not reasonable because they represent more than one-
21 third of the total amount sought by the Trustee.

22 The billing records for the legal fees sought by the
23 Trustee in this category are contained in the Declaration of
24 Denice Moewes in support of the Trustee's Third Application for
25 fees. That application documents \$88,845 in fees incurred as
26 of April 30, 2008. The Court has reviewed the time entries in
this category and does not believe the fee request is

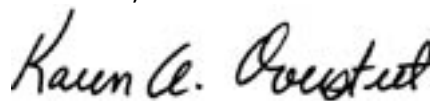
1 unreasonable. Trustee's counsel was required to sift through
2 boxes of documents and to piece together which documents Herman
3 Recor had at relevant periods of time and which documents were
4 not produced. The Trustee's attorneys worked with
5 Mr. Levenhagen to recreate the events that took place over the
6 course of the litigation and to document those events in
7 multiple exhibit binders for the Court. The briefing related
8 to the Sanctions Motion is very significant. The Court finds
9 that the investment of the Trustee's attorneys' time was
10 necessary to adequately present this complex matter to the
11 Court.

12 Because the Trustee has only documented \$88,845 in fees,
13 however, the award is limited to that amount until further
14 billing support for the additional services performed
15 subsequent to April 30, 2008 is provided.

16 CONCLUSION

17 For the foregoing reasons, the Court will enter an order in
18 favor of the Trustee requiring reimbursement from Herman Recor
19 for discovery violations and abuses in the amount of
20 \$94,514.43, plus legal fees incurred in bringing the Sanctions
21 Motion in the amount of \$88,845. The Trustee may seek
22 additional fees incurred after April 30, 2008 by supplemental
23 motion.

24 Dated this 27th day of October, 2008.

25 

26 Karen A. Overstreet
U.S. Bankruptcy Judge

McCarty v. Global, et. Al.	EXHIBIT A	
Sanctions Motion Fee Analysis		
Fee Category		
Discovery	Court allowance	Trustee's Request
1/9/2007	55.00	
1/10/2007	82.50	
2/1/2007	310.00	
2/2/2007	1,364.00	
2/21/2007	220.00	
2/22/2007	1,045.00	
2/23/2007	357.50	
2/23/2007	62.00	
10/31/2006	52.00	
11/6/2006	52.00	
11/7/2006	885.00	
11/7/2006	884.00	
11/15/2006	1,014.00	
11/16/2006	2,065.00	
11/16/2006	2,288.00	
12/6/2006	100.00	
12/8/2006	546.00	
3/5/2007	907.50	
3/8/2007	165.00	
3/8/2007	150.00	
3/9/2007	852.50	
3/16/2007	82.50	
3/18/2007	330.00	
3/19/2007	412.50	
3/20/2007	130.00	
3/25/2007	400.00	
3/26/2007	192.50	
3/26/2007	27.50	
3/27/2007	247.50	
4/1/2007	1,925.00	
4/2/2007	3,712.50	
4/2/2007	28.00	
4/2/2007	112.50	
4/2/2007	10.50	
4/4/2007	200.00	
4/5/2007	330.00	
4/6/2007	192.50	
4/13/2007	330.00	
4/18/2007	27.50	
4/23/2007	55.00	
5/1/2007	137.50	
7/25/2007	165.00	
10/23/2007	27.50	
10/26/2007	110.00	

10/29/2007	1,485.00	
10/30/2007	1,897.50	
10/31/2007	2,200.00	
Total Discovery	28,225.50	44,608.00
First Motion for Summary Judgment	32,414.50	32,414.50
Second Summary Judgment Motions	7,081.00	7,081.00
Trustee's Motion (vacate order)	0.00	25,968.00
Trustee's Motion vs. Levenhagen	25,098.00	25,098.00
Expenses: aborted depositions	1,695.43	1,695.43
Total Damages	94,514.43	136,864.93
Fees assoc. with Sanctions Motion	88,845.00	95,174.50
Total Court Award	183,359.43	
Trustee's Request		232,039.43